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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1965

No. 402

In The Matter of
Rosenberg Iron & Metal Co., Inc.,

Bankrupt.

DEMPSTER BROTHERS, INC.,

Petitioner

vs.

MILTON M. COHN, Trustee in Bankruptcy,

Respondent.

**On Petition For Writ Of Certiorari To
The United States Court Of Appeals For The Seventh Circuit**

BRIEF FOR RESPONDENT IN OPPOSITION

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HAMMERSMITH-KORTMEYER CO. MILWAUKEE

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QUESTIONS PRESENTED

(1) Is the decision of the Seventh Circuit Court of Appeals in the case at bar contrary to the decision of this Court in the case of *Lewis v. Manufacturers National Bank of Detroit,* 364 U.S. 630, 81 S. Ct. 347 (1961)?

(2) Is the decision of the Seventh Circuit Court of Appeals in the case at bar in conflict with the decision of the Ninth Circuit Court of Appeals in the case of *Pacific Finance Corporation v. Edwards,* 304 F. (2d) 224 (9th Cir. 1962)?

ARGUMENT

I.

The decision of the Circuit Court of Appeals is not contrary to the decision of this Court as set forth in Lewis v. Manufacturers National Bank of Detroit, 364 U.S. 630, 81 S. Ct. 347 (1961)

In support of its petition for a writ of certiorari, the appellant asserts that the Seventh Circuit Court of Appeals in arriving at its decision in the case at bar, ruled contrary to the holding in *Lewis v. Manufacturers National Bank of Detroit,* 364 U. S. 630, 81 S. Ct. 347 (1961). In support of this argument, appellant cites extensively from the *Lewis* case and then goes on to state, at page 6 of its brief, that:

> "The trustee in the case at bar is attempting to reach back to the period of June 19, 1961, to June 26, 1961, and claim that during this eight day period of non-recordation a creditor of Rosenberg Iron & Metal Co. could have obtained a lien and, therefore, the trustee on October 18, 1961, the date of bankruptcy, is clothed with the power of such a creditor and his status as of June 19, 1961, to June 26, 1961.
>
> This position advocated by the trustee and approved by the Circuit Court of Appeals is contrary to the holding in *Lewis v. Manufacturers National Bank of Deroit,* 81 S. Ct. 347."

We respectfully submit that the position as set forth above by the appellant is not the position of the trustee nor was it the basis of the Court of Appeals decision. If we, for the sake of analysis, disregard the existence of the state court restraining order, then it is clear

that a hypothetical lien creditor as of the date of bankruptcy could have obtained a lien superior to that of Dempster Brothers, Inc. because of Dempster Brothers' failure to refile its conditional sales contract in accordance with the provisions of Section 122.11, Wis. Stats. (1961). The appellant takes the position that by reason of the existence of the state court's restraining order, no creditor, actual or hypothetical, could have obtained a lien as of the date of bankruptcy. Therefore, the appellant reasons, the court's holding that the trustee by virtue of 70(c) takes a position superior to that of Dempster Brothers means in essence that the trustee can reach back to the period subsequent to the time the filing lapsed but prior to the time of the state court restraining order.

While the Court of Appeals did distinguish the case at bar from the *Lewis* case on the factual basis that the anterior point of time referred to in the *Lewis* case was the period between the date the loan secured by the chattel mortgage was made and the date the chattel mortgage was recorded, whereas the anterior point of time in our case was posterior to the expiration of the three-year filing period, the distinction made was not necessary to the Court's decision, nor does it imply any deviation from the holding of the *Lewis* case. On page 503 of its decision, the Court stated:

> "It is conceded that Dempster did not refile its conditional sales contract and that the three-year filing period expired June 18, 1961. Unquestionably, then, the initial filing could not operate against those who extended credit to Rosenberg after that date. We agree with the referee that the trustee under the provisions of section 70(c) acquired as of October 18, 1961, the status of a creditor who without notice of the conditional sales contract extended credit to Rosenberg after June 18, 1961, and then obtained

> by levy or attachment a lien upon the baling press, and that this is so regardless of whether such a creditor actually existed."

From the foregoing language, it is apparent that the Court's decision is premised upon the proposition that a creditor who had a lien as of the date of bankruptcy would have had lien rights superior to those of Dempster Brothers and, therefore, the trustee is vested with such lien rights pursuant to Section 70(c) of the Bankruptcy Act.

We think it significant to note that although the appellant contends that the state court's restraining order precludes the trustee from exercising the rights vested in him pursuant to Section 70(c) of the Bankruptcy Act, it has failed to cite any authority in support of its contention or any authority setting forth the effect of a state court's restraining order on the rights granted the trustee in bankruptcy. While the respondent has also been unable to locate any authority on these points, we believe that certain observations concerning the power of a state court receiver and the power of the bankruptcy trustee would be helpful in resolving this issue.

A state court receiver is granted almost identical rights under Sec. 128.18(1), Wis. Stats. (1961) as are granted to the trustee in bankruptcy under Sec. 70(c). Section 128.18(1), Wis. Stats. (1961), provides:

> "Claims which for want of record or for other reasons would not have been valid liens as against creditors of the debtor armed with process, pursuant to which said property has been attached or levied upon, shall not be liens against the estate."

Pursuant to the provisions of Sec. 128.18(1), Wis. Stats. (1961), the state court receiver would have enjoyed rights

superior to those of Dempster Brothers, Inc. See *In Re Adams Machinery, Inc.*, 20 Wis. (2d) 607, 123 N.W. (2d) 558 (1963).

The position advanced by the appellant means that the conditional sales contract would be void as to the receiver under Wisconsin law and also void as to the trustee under Section 70(c) of the Bankruptcy Act if a state court receiver had not been appointed but, because of the appointment of the state court receiver and the issuance of a restraining order, the trustee lost his rights under Section 70(c). Such a determination would result in an inequitable treatment of creditors and be contrary to the very equitable nature of these proceedings. Furthermore, holding that the appointment of the state court receiver and the entry of a restraining order deprived the trustee of his rights under Section 70(c), and also deprived all creditors of their rights, would mean in essence that the appointment of the state court receiver, the entry of the restraining order and the subsequent adjudication of bankruptcy perfected the lien of Dempster Brothers, Inc. as to subsequent creditors and as to the trustee; something which Dempster Brothers, Inc. could not have done itself under Wisconsin law. Such result would not be in keeping with the rationale of Section 70(c).

II.

No Conflict exists between the Decision of the Seventh Circuit Court of Appeals and that of any other Court

The appellant also alleges in its brief in support of its petition for a writ of certiorari, that the decision of the Court of Appeals in the case at bar is contrary to the decision of the Ninth Circuit Court of Appeals in the case of *Pacific Finance Corporation v. Edwards,* 304 F.

(2d) 224 (1962). In the decision in the *Pacific Finance Corporation* case, the Ninth Circuit Court of Appeals held that the trustee could not exercise the powers given to him in Section 70(c) of the Bankruptcy Act unless there was an actual creditor in existence at the time of bankruptcy who could have obtained such a lien. The appellant takes the position that the state court restraining order in the case at bar precluded any creditor from obtaining such a lien and, therefore, the decision that the trustee by virtue of Section 70(c) takes a lien superior to that of Demptser Brothers, is contrary to the decision of the Ninth Circuit Court of Appeals in the case of *Pacific Finance Corporation v. Edwards,* 304 F. (2d) 224 (1962).

The appellant in raising this contention does not allege that there was no actual creditor in existence who might have obtained a lien. What the appellant does allege is that the state court restraining order would have prevented such a creditor from obtaining a lien and therefore there was not an actual creditor in existence who could have obtained a lien as of the date of bankruptcy. We submit that the appellant is attempting to extend the holding of the *Pacific Finance* decision beyond what was decided in that case. That case did not require more than that an actual creditor exist who under a hypothetical situation could obtain a lien of the type described in Section 70(c). It did not take into account the ability or inability of an actual creditor to perfect the lien by reason of valid or invalid court orders, State legal holidays on the date of bankruptcy, or other procedural impediments which an actual creditor might encounter. In order to argue that a conflict exists between the Seventh Circuit and the Ninth Circuit, it is necessary to show that there was no actual creditor in existence who under ideal con-

ditions could have obtained a lien superior to Dempster Brothers, Inc. as of the date of bankruptcy.

On page 12 of its brief, the appellant admits that there was a creditor in existence who extended credit to the bankrupt subsequent to the time when the filing of the conditional sales contract lapsed. The appellant, however, contends that the mere existence of such a creditor is not sufficient and that the burden of proof is upon the trustee to show that such creditor had no knowledge of the reservation of title by Dempster.

It is the trustee's position that in Wisconsin the burden of proof to show that a creditor who extended credit to the bankrupt subsequent to June 18, 1961 had notice of the conditional sales contract is upon the appellant, Dempster Brothers, Inc., and that the appellant has failed to sustain this burden. Appellant cites the case of *In Re Douglas Lumber Company,* 2 F. (2d) 985 (1924) in support of its position. The *Douglas Lumber Company* case is distinguishable from the case at bar. In the *Douglas* case the Supreme Court of Wyoming held that under a Wyoming law the burden of proof was upon the person claiming against the vendor to show that he did not have notice. Therefore, by reason of the wording of the Wyoming statute, the District Court was constrained to follow the Wyoming law on this matter. Such is not the law in Wisconsin. In the case of *New Dells Lumber Company v. Pfiffner,* 216 Wis. 638, 258 N.W. 375 (1935), a conditional seller brought an action against a conditional buyer and his mortgagee to recover the value of certain sleighs. The Court, in discussing the question of whether the evidence established that the mortgagee had notice of the agreement reserving title in the vendor, stated at page 644:

> "We think it clear that, unless it be shown that a purchaser . . . had actual knowledge of such facts

> as would put a prudent man upon inquiry, which, if prosecuted with ordinary diligence, would lead to actual notice of the right or title in conflict with that which he is about to purchase, a conditional sale contract would be void as to him."

It can be seen from the language of the Court that the Court contemplated that the burden of proof would be upon the vendor of the conditional sales contract to show that a subsequent purchaser or creditor had notice of the said contract.

The appellant also cites as authority for its position the concurring opinion in the case of *In Re Masters Knitting Corporation,* 7 F. (2d) 11 (2nd Cir. 1925). The majority opinion disagreed with the concurring opinion on the question of the burden of proof and held, at page 12:

> "Let it be assumed that, if all the creditors of this bankrupt knew that this sale was conditional, the petitioner below should prevail; it remains true that the trustee has the right of any creditor and the burden of proof is on the conditional vendor to prove no creditor was without notice."

From the foregoing it can be seen that there was an actual creditor in existence who could have obtained a lien superior to that of Dempster Brothers, Inc. Since there was an actual creditor in existence who under Wisconsin law could have obtained a lien subsequent to the date when the filing period lapsed, the decision of the Court of Appeals in the case at bar is not contrary to the holding of the Ninth Circuit in *Pacific Finance Corporation v. Edwards.*

Finally, on pages 15, 16 and 17 of the appellant's brief, the appellant appears to argue that since failure to refile a conditional sales contract destroys its validity only as to subsequent creditors who have obtained a lien without notice of the existence of the conditional sales contract, and since there is no such lien creditor in existence, the trustee is not vested with the rights of a lien creditor pursuant to Section 70(c) of the Bankruptcy Act.

While it is true that there is authority to the effect that there must be an actual creditor in existence on the date of bankruptcy who could have obtained a superior lien in order for the trustee to be deemed vested with such a lien by virtue of Section 70(c), there is no authority that there must be an *actual* lien creditor in existence. The decision in *Pacific Finance Corporation v. Edwards,* 304 F. (2d) 224 (9th Cir. 1962), at page 228 stated:

> "Under our construction of §70, sub. c the trustee is empowered to exercise the powers given him even if no actual creditor has obtained a lien, but he cannot do so if no actual creditor could have obtained a lien."

CONCLUSION

Respondent respectfully submits that for the reasons heretofore set forth, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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